



1998 Report: Problem Areas

June 4, 1998

Pursuant to Section 77-5012, R.S. Supp. 1997, the Tax Equalization and Review Commission (hereinafter referred to as the Commission) shall, "publish a formal equalization plan.. The plan shall focus on problem areas both geographically and by type of property as indicated by the Property Tax Administrator.. ." The hearings conducted by the Commission for the formal plan commence on May 28, 1998, therefore the Property Tax Administrator (hereinafter referred to as the Administrator) is issuing the 1998 Report: Problem Areas, in a timely manner for consideration by the Commissioners and other interested persons.

In a format similar to the 1997 Report: Problem Areas, the 1998 Report will summarize the findings of the Administrator focusing on problem areas both geographically and by type of property in compliance with Section 77-5012, R.S. Supp. 1997. The 1998 Report will also provide general information regarding the efforts of the Property Tax Division (hereinafter referred to as the Division) in preparation for the 1999 assessment year, focusing on improvement of assessment practices and development of the sales file used to publish assessment ratio studies and other statistical measures.

The purpose of the Division is to assist the Commission and other interested persons in accurately measuring the efforts of the county assessor in setting uniform and proportionate values on real property for tax purposes in each county, and to provide useful information to the county assessor to facilitate their efforts. Additionally, state law requires the Division to adjust the assessed valuation of each school district for use in the Tax Equity and Educational Opportunities Support Act and to publish assessment ratio studies to measure the quality and uniformity of assessment practices. (Sections 79-1016 R.S. Supp. 1997, and 77-1327, R.R.S. 1996.)

HIGHLIGHTS FROM THE 1998 EQUALIZATION PROCESS

For the 1998 assessment process, the Division continued to devote considerable time and effort in the development of the sales file, which was used to create statistical studies to indicate the quality of assessment and level of values of the classes and subclasses of real property in each county. Additionally, the Division continued its efforts to understand the assessment practices of Nebraska's 93 county assessors. Testimony of individual counties gave insight to the various steps that the counties are taking on their own initiative and often without additional staffing and funding. Several indicated that they have taken steps toward improving their assessment records through reallocation of their time to review each property individually. Although these efforts were not immediately rewarded, the results will obviously be beneficial in the years to follow. These actions are, as the Commission stated, commendable. The Division will borrow from these initiatives to facilitate actions in other interested counties.

DEVELOPMENT OF THE SALES FILE

While the Division has managed a sales file used to measure the level of value of classes and subclasses of real property in the state for several years, continued heavy reliance upon the data raised concerns and questions regarding the process. The data displayed was used by many county assessors to plan and implement adjustments to the assessed value of classes and

subclasses of real property in the county, by the Commission to make adjustments of classes and subclasses of real property for purposes of statewide equalization. and will be used to adjust the assessed valuation of real property in each school district for purposes of state aid.

As in 1998. and in order to facilitate planning for the 1999 assessment process. the Division shall adhere to a strict schedule for the transfer of information from the county officials to the Division for the sales file development. For the 1999 assessment year. the Division will take action to assure that the sales file is adequately and timely developed. The Administrator will issue a directive within the next month that will specify the process for the transfer of information used in the sales file, the responsibilities of the Division and the county assessors in the review of the data, and the ability of the county officials to challenge the actions of the Division regarding the data used in the sales file. The purpose of the directive is to develop the sales file through a systematic process. to give advance notice to all interested persons regarding the process. and to serve as a mechanism to assure compliance with the process. Without such a directive. the sales file cannot be timely developed for use in the 1999 assessment and equalization process.

The Property Tax Division will be reviewing the sales of commercial and industrial properties. and agricultural properties, improved and vacant. as in previous years. While relying on the services of professional appraisal services in the past. the Division will be conducting the review process "in-house" employing qualified staff sufficient to cover each area of the state. The anticipated start-up date for this endeavor is July 1, 1998: however, creating and staffing these positions is subject to fulfilling the requirements of the office of State Personnel. This change in procedure has cost several months of lost time in the continuity of the review process. but is considered a resolution to concerns raised in regard to the quality. consistency. and control over important determinations in regard to qualification and non-qualification of the sales used in assessment analysis.

Of particular concern is the proper coding of the sold properties to match the classifications for unsold properties so that adjustments will be applied to the proper class and subclass of property. This is also important when calculating the percentage change for the sales file in comparison with the value changes in the abstract. This issue was raised many times during the statewide equalizations. Several counties testified to the Commission that through misunderstanding of reporting assessed values, the sales used in the analysis were being compared to assessed values of improvements made to a parcel of land that were not in existence or were not assessable at the time of sale. In several instances, the corrections to the county rosters are made by clerical staff that are not given guidelines on when to include or exclude new valuation, growth, or changes in assessment which are not reflective of the property as sold. Steps will be taken for 1999 to resolve these issues so that the statistics presented to the Commission will be truly representative of the county and not subject to question, change, or adjustment.

The Property Tax Administrator will promulgate revised regulations for appraisal and assessment practices for 1999. These regulations will clarify the proper "coding" of sales for stratification of the assessment studies. Other areas addressed will include proper review of the sales "qualified" as arms-length in nature. The initial determination must be made as to whether the transfer statement represents a bona-fide sale or is just indicative of some other form of transaction. In an Assessment Journal article entitled "A New Approach to the Analysis of Assessment Equity", the authors state that sample bias is often the result of inaccuracies in the

inventory of the real property (the specific data). infrequent revaluations, and nonrepresentative samples used in measuring assessment practices:' however; there exist anomalies in the inefficiencies of the real estate market. The existence of these irregularities is inherent in the market and not necessarily an indication of assessment bias on the part of the county assessor. These occurrences must be kept in mind in any analysis of empirical data. The representativeness of the sales to individual properties has existed in the past. while it may be more appropriate to consider these statistics as a barometer of what is happening in the county as a whole. The appropriateness of applying general data to specific properties should be considered. The expectation of all counties to meet the "quality" statistics of price related differential and coefficient of dispersion regardless of the size of the county and the sample size of sales continues to be a concern. The IAAO standard makes reference to these tests being applicable to a representative sample of homogenous properties and recognizes the limitations of applying the standard in jurisdictions that may not have a representative sample to draw from for statistical analysis. The Commission has recognized this in their determination that improving the assessment of a county by applying a percentage adjustment to a class or subclass may result in an acceptable median level of value, but the result will not create better equalization within the class or subclass itself.

The process established by the Administrator will be rigorous. and adherence to the schedule will be mandatory for all officials both state and local. in the development of the sales file. If the process is followed, the sales file will be a useful tool at all stages of the assessment of real property for tax year 1999.

REPORTS OF THE PROPERTY TAX ADMINISTRATOR

Several reports will issue from the Administrator during the 1999-assessment process. The reports, including statistical data, are intended to provide the Commission and the county assessors with information that will illustrate the progress made in the improvement of the assessment practices of real property.

The Division will conduct interviews with each county assessor during September, 1998, the purpose of which will be to gather information regarding the structure of each county assessor's office, the actual budget of the county assessor's office for the 1998-99 fiscal year, and the assessment plans of the county assessor for the 1999 assessment year. The information will be compiled and made available to the Commission as soon as it is compiled. It is anticipated that this report will assist the Commission in having data on the funding and resources available to the county assessors and the plans anticipated to be carried out for the assessment of real property for 1999.

The Division will provide statistical data to the Commission and the county assessor twice during the 1999 assessment process; first, in early January, 1999, and second, on or before April 5, 1999. The first statistical reports will display the assessment ratio and other related statistics of the county by class and subclass prior to the implementation of the 1999 assessed valuations. The second statistical reports, which will accompany the "Opinion of the Administrator", will display the assessment ratio and other related statistics of the county by class and subclass after implementation of the 1999 assessed valuations. Additionally, the data will be displayed in two reports for each class of real property: first, the analysis of the sales in the data base limited only to the qualified sales; and, second, the analysis of all sales in the data base, excluding the top and

bottom ten percent of the sales. The purpose of this information is to provide the Commission with benchmark data from which to review changes made to assessed valuations by the county assessor for the 1999 assessment year. The format of the report will be changed in order to provide information more relevant to the Commission's responsibility of adjusting by class and subclass. One change may be made to the analysis by "subdivision" which has not been relied upon to make adjustments. This category will be replaced by an analysis of improved, unimproved, and improvements on lease land subclasses (status) for residential property. These subclasses have been considered for adjustment in the past.

MANAGEMENT OF THE ASSESSMENT PROCESS

It continues to be the opinion of the Administrator that the offices of the county assessor are severely understaffed and under-funded. There is great disparity in the availability of technological tools available to each county assessor. And while some offices may be adequately funded and staffed in the opinion of the county assessor, there is an issue of the dedicated use of the resources available for the county assessor for the assessment of real property. As it has often been stated by observers of the assessment process to gain real progress in the quality of the assessment of real property the resources must be made available at the source of the valuation process, the county assessor, and those resources must be focused upon the assessment and valuation of real property. To put resources into any later step in the process diminishes the return on the investment to the assessment process; however, many assessors are developing systematic assessment programs utilizing the limited resources available. These efforts are not seen as a "quick fix", and immediate gratification may not be realized. As the counties continue to make progress in their assessment responsibilities the results of their efforts should make a lasting affect for future valuations. The Property Tax Division should be a responsible facilitator of the sharing of ideas and processes which will improve assessment.

As of December 31, 1997: the county boards of five counties resolved to transfer the assessment functions of the county to the Property Tax Administrator and the Property Tax Division. Acceptance of the transfers has been mixed from both the elected officials' viewpoints and from taxpayers' views. Since that time the Division has been busy determining the needs for continuing the assessment practices already in place and determining what, if any, changes are needed to operate the offices of the county assessors in a more proactive manner. Such issues as the rights of the new employees, salaries, equipment, existing contracts and relationship to existing county offices and processes have been researched. The Division is planning for the new responsibility to be effective July 1, 1998, with as few disruptions as possible. The new responsibility puts additional responsibility on the Division, but affords the opportunity to realign duties of existing staff such that individual counties could not have accomplished. The education and experience of the new staff members should make it possible to put their talents to better use in a wider area and assist the Division in meeting other assessment objectives and responsibilities.

INVENTORY OF PROPERTY CHARACTERISTICS

A continued area of concern, and one that was raised during the hearings of individual property appeals to the Commission and during the hearing for statewide equalization, is the fundamental

process of listing accurate, current and pertinent characteristics of real property from which to make a determination of the market value of the real property in the county. While an accurate and current listing of the property's characteristics will not guarantee quality assessed valuations, it is certainly necessary to make an efficient use of the market data. Without an accurate and current inventory capturing all characteristics that effect value in the market, development of comparability of sales is seriously impeded. Also, initiating and maintaining a current inventory of property characteristics and a uniform standard of applying subjective characteristics establishes a factual threshold of reasonability of valuation that must be overcome in any challenge to the valuation of real property in the county. Referring, again, to the Assessment Journal article, the inaccuracies of the "cadastre" contribute to sample bias and misinterpretation of the assessment analysis. The "cadastre" includes the identification and classification of the general and specific data in the assessment process. Several counties, recognizing that they will continue to be plagued by this outdated information, have taken the initiative to systematically review each parcel in the county to correct inadequacies of their current records as they prepare the 1999 assessments.

THE COST APPROACH

One issue that was questioned in several hearings of statewide equalization was the issue of the date for the information used in the cost approach. The use of out-of-date cost estimates results in newer construction being placed on the tax roll at below current costs. Variances within a county in the dates of the manuals used to establish the replacement cost estimates raise concerns in the failure to establish accurate market derived depreciation factors, also. Except in cases when the cost information (specific data) has become outdated, the cost information can be adjusted to arrive at a reasonable estimate of replacement cost new by appropriate use of cost trend multipliers. Cost estimates should be more uniform both within the county and in counties with overlapping tax districts to promote fair and equitable assessments.

MOBILE HOMES/VACANT LOTS

Section 77-103 (R.S.Supp. 1997) defines real property as, "All land, all buildings, fixtures, and improvements: mobile homes, cabin trailers, and similar property, not registered for highway use..."

Another area of continued concern is the listing of the mobile home sales and vacant lots with other residential properties in the assessment sales ratio studies. These subclasses of residential property continue to reflect volatility in the market. The concern is that the ratio calculated using these sales indicates poor assessment practices that are not representative of the general class of residential properties. Comments from assessors infer that many of these sales occur without the aid of professional real estate sales people. The result is that the market prices paid may vary greatly depending on the immediate needs of the market and can reflect substantial differences within the same community within a few months', weeks', or days' time. Indications are that due to the lower quality of construction and the intensive use of mobile homes, there are problems in determining the "effective age" essential to estimating accrued depreciation. The county assessors association is considering taking steps that could help equalize the values in the assessment process, but which may not guarantee that the value is set at 100% of market for

every transaction observed. The Property Tax Division will continue to display the statistics for these types of real property recognizing that this is not to be viewed as an indictment of the assessment practices of the county.

"PICK-UP" WORK

Evidence regarding the current listing of property characteristics will again be investigated by the Division in the information gathered from the county assessors. The process of gathering information to accurately list real property for the assessment roll includes the process commonly referred to as "pick-up work." Pick-up work is the annual process of listing for assessment the real property added to or removed from the roll in the last year, and includes new construction and modifications to improvements or rezoning of existing real property. Specific information regarding the requirement for building permits or the use of the documents required by section 77-1318.01, R.S. Supp. 1997, will be investigated. As stated in the 1997 Report the failure to annually update the assessment roll with pick-up work leads to substantial undervaluation within the assessment jurisdiction, not to mention violation of the requirement of uniform valuation and non-commutation of tax provisions of the Nebraska Constitution.

Testimony before the commission indicated that several counties were performing some of the "pick-up" work in conjunction with their sale verification procedure. While this is a commendable step upon the part of the assessor in updating the specific data on the property in an efficient manner, it raises concern over whether other "unsold" properties are receiving the same attention. The net effect may indicate that the county is adjusting only sold properties.

APPRAISAL CONTRACTS

Many counties will undertake the process of reappraisal of classes or subclasses of real property within the county. While the Division is required by law to approve all reappraisal contracts, in no manner is the Division involved in assuring that the reappraisal work meet specified standard. The county must protect itself from any inadequate work. However, as suggested by the Commission in hearing during statewide equalization, one requirement that the county contract should include is the requirement that assessed valuations of all reappraised real property achieve the standards required in General Order Number 6 of the Commission.

COMMERCIAL AND INDUSTRIAL REAL PROPERTY

While commercial real property and industrial real property has been analyzed separately, there is evidence that might support combining the statistical analysis of the sales of these properties for future consideration. Several counties testified, in fact, that they had difficulty in distinguishing between these two property uses. The specific example was in the heating, ventilating and air conditioning business, in which the company was of a commercial enterprise, but also manufactured goods to specific needs of their customers. In order to comply with the zoning ordinances of the community, the business was required to be in an area zoned for light industrial use. An apparent confusion arises, then, as to whether the analysis should be based on the "use" encoded or the "zoning" encoded. For purposes of this report the problem areas of these two classes will be discussed together, as the problems are identical.

This class of real property provides the fewest number of sales from which to develop market value which is recognized as a cause for sample bias in statistical analysis. It is by far the least actively traded class of real property. Additionally, these sales more likely than not, do not represent arms length transactions and the selling prices are significantly effected by factors beyond the value paid for real property. Commercial and industrial property presents several challenges for 1999: low number of sales statewide; inconsistent classification of the property sold; and, proper subclassification within the county.

Commercial and industrial real property analysis has historically caused the most concern for the division in developing the level of value for a county. Our historic answer has been to rely on the presumption that the county assessor has properly valued this class of real property, and to assume it is valued at 100% of market value. The Division will maintain three years of sales information for commercial and industrial real property in case this information would provide guidance regarding the level of value of these classes of real property.

AGRICULTURAL LAND

This class of real property provides a sufficient number of sales from which to develop market value. The assessment of this class of real property was more restrictively governed by statute; however, with the adoption of LB 270 the statutory restrictions have been repealed. This legislative change should make it easier to recognize the market valuation influences within the agricultural land market, thereby providing additional opportunities for the county assessor to achieve market value. The division shall modify its output to *more* adequately display the statistical information representing a county assessor's use of market areas. The challenges in the valuation of agricultural land for 1999 include low number of sales within a class or subclass in a county; uniform classification of the land; and, recognition of agricultural versus nonagricultural influences in the market for rural land. In several counties, special valuations ("greenbelt") for agricultural land have been applied on qualified parcels in order to defer the taxes until the land no longer qualifies based on zoning, subdivision, or use. This method has been considered for valuing other land that is selling for recreational use and land in areas with "scenic river" designations.

It is the Division's opinion that when the policy of valuing agricultural land changed to market value, reliance upon the detailed classification and value structure from the prior policy became obsolete. As stated earlier, classification is an important process in the assessment function, but it does not guarantee quality valuation. Since agricultural land crosses every county line in this state, across-county line comparisons are valuable tools in the statewide equalization of this class of real property. The classification method required by the Division is contained in the Nebraska Agricultural Land Valuation Manual and is based on the policy that consistent classification will allow for accurate across-county line comparisons. This uniform classification will also allow for the easy sharing of sales information from one county to another in similar areas of the state. It is the position of the division that each county that has not implemented the soil conversion contained in the 1998 manual must implement the conversion for the 1998 assessment year. The land values presented in the manual represent a general target for the valuation of the classes of agricultural land. The county assessor must apply appropriate values within the county, or areas within a county, based upon their review of the market for agricultural and horticultural land.

Following the mandatory classification of agricultural and horticultural land as set forth in the manual guidelines, enables accurate plotting of the sales so that the county assessors can get guidance in valuing the property through their Field Liaison. The Field Liaisons are also instrumental in coordinating the valuation effort between adjoining counties and should offer assistance to the Agricultural and Horticultural Land Valuation Boards. These AHLV Boards are still experiencing confusion on what specific responsibilities and powers they have in the valuation and equalization of agricultural land. The confusion and frustration culminated in introduction of legislation that would have eliminated the Boards and the land manual areas established in statute. While appearing to be a rather drastic measure, it points out the need for providing the AHLV Boards with more direction and guidance either from the Tax Equalization and Review Commission or the Property Tax Administrator. The Property Tax Division was pleased that several commissioners accepted an invitation to attend the Assessors Administrative Workshop in February, 1998. This effort will continue for the 1999 assessment year.

Other issues of concern regarding agricultural land are similar to those raised in the 1997 Report, including an accurate inventory of the soil types, which form the basis for the classification of agricultural land and recognition of the various market areas of agricultural land in the county. Focus on these issues must continue to be explored to assure that the valuations are proportionate both within the county and among the counties.

GEOGRAPHICALLY DEFINED ISSUES

The issue of the valuation of improvements located on land that is leased continues to be debated. The Commission has heard testimony regarding recreational property, in the sense that there are areas within the county designated as recreational areas, such as lakes, rivers or other geographically desirable locations (as opposed to classification of an improvement as recreational). The issue presented is the attempt to recognize the market valuation of these improvements that are, in some cases, dramatically affected by the location in the recreational area. The position of the Division is that the market value of these specially located properties must be recognized so that all parcels of real property will pay a proper proportionate share of the property taxes assessed. Additionally, the valuation of the improvement must recognize the entire bundle of rights, or as stated in statute, "all privileges pertaining to real property", associated with the improvement, not just the value of the improvement itself. (Section 77-103(5), R.S. Supp. 1997)

Another issue concerns the valuation of accretion land. Issues regarding rights of ownership have arisen concerning land that has accreted to adjoining land along rivers in certain areas of the state. The market gives an indication of marketable title, while restrictions on private ownership in these areas exist. This concern is closely related to the other in that it usually involves recognition of a value tied to the "recreation" potential of the property. The county may establish these areas as individual market areas for which separate values could be established. As indicated in the hearings, these areas often do not meet the standard of being assessed at 80% of market value. The division needs to work closely with the county assessors in these areas to determine issues of both ownership and valuation.

CONCLUSION

The 1998 Report summarizes many issues for the Commission's consideration. The administrator and the Division will focus on providing information and assistance to resolve many of the concerns that have been expressed regarding the 1998 assessment process. We pledge our commitment to facilitating improvements outlined in the 1998 Report and issues raised by the Commission in the formal plan of equalization.